UNITED STATES DEPARTMENT OF AGRICULTURE
Economic Research Service
Resource Development Economics Division
Area Economic Development Branch

CONDITIONS CONDUCIVE TO ECONOMIC DEVELOPMENT IN LOCAL AREAS

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Prepared for delivery before
The Eleventh Annual Farm Business Training Conference
Stillwater, Oklahoma
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Gold is where you find it.--Miner's adage.

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The search for a conceptual base for economic development--either local or national--is in one sense easy and in another sense difficult. As with the search for other knowledge, it is difficult to entirely miss the mark and to shed no light upon the process. But on the other hand, it is virtually impossible to encompass the entire phenomenon.

In saying that the search is in one way easy and in another difficult, it is the burden of this paper to suggest that despite what you may have heard from other economists, there are considerable opportunities for the development of local areas well outside the metropolitan centers. In this sense, the message of the paper is optimistic. However, I do not mean to in any way minimize the difficulties now confronting local areas. The development path ahead is at best uncertain and frustrating.

Some economists have pointed out that during the past two decades, economic development and employment have increased more rapidly in the metropolitan areas. The urban-industrial hypothesis explicitly suggests that there is a direct relationship between the rate of growth of industrialization and urbanization and the local levels of income in rural areas. It is my suggestion, which in no way contradicts the observed development of the past twenty years, that there is a danger in the oversimplification of this hypothesis. What I mean to say is that employment and investment opportunities

exist and will continue to exist in communities of all sizes. The mere placing of an investment in a metropolitan community does not insure its success, any more than placing it in a smaller one insures its failure. One has only to look at the bankruptcy columns of any major city newspaper to see evidence of this. On the other hand, we now have observed that many enterprises, both new and old, flourish in areas of far smaller population concentration. The real test of the success of a particular investment is its survival. It behooves us not to overgeneralize the phenomenon of more rapid growth in the larger centers. This means that investment opportunities in the smaller centers should not be left unexploited.

OBSTACLES TO DEVELOPMENT IN SMALLER COMMUNITIES

It is, of course, true that the search for investment and employment opportunities in the smaller centers is generally more difficult than the search in more populous areas. In the first place, family incomes in agriculture, in spite of extensive agricultural programs, continue to be smaller than incomes to persons of similar capacity in more urbanized communities. This means that there are less aggregate earnings for the stimulation of either the production or consumption of goods and services. Moreover, the local accumulation of capital for investment purposes will have to come out of smaller and more widely dispersed incomes. Although farmers have been conspicuously successful savers, there is no escaping the unfortunate fact of a low income base. National capital markets are by no means so perfect as to correct all deficiencies in local capital availability.

In the second place, since various economic alternatives in the larger centers are more satisfactory than those in smaller ones means many local areas, perhaps half the counties in the country, have lost

population during the last ten or twenty years. This loss of population acts as a brake to development in these areas in that the dependency ratio, the relationship of those of more or less than working age to the working adult population, becomes disadvantageous. At the same time, the continued outflux of population results in a considerable drain upon the economy in that these persons have been educated at local expense. A glimpse of any of the statistical age distributions shows considerable decrease of persons after they reach 18 years of age. On the other hand, there are disproportionately larger numbers of persons in the older ages, say between 45 and 70. This does not mean that the only burden of this age structure is borne by the public sector. Every local family in its private capacity bears some of this weight.

In the third place, agriculture in most areas is undergoing a considerable reorganization, stemming, at least in part, from the general population exodus. This fact carries in it the seeds of opportunity, as well as some major burdens. In terms of simple capital availability the process of paying off nonfarming brothers and sisters for the inheritance of a farm indicates a considerable off-farm movement of capital arising from the very process of farm reorganization.

A fourth problem relates to the improvement in communications and transportation systems. Although perhaps recognized intellectually, the economic impact of the development of the interstate highway system is, I believe, coming as a considerable surprise to many persons in local areas. On the positive side persons may continue to live in a farm household and be employed in urban areas considerably removed. They may do this either as part-time farmers or simply as employed wives or children of farmers. On the

adverse side, from the point of view of local businesses the availability of modern, high speed highways means that a smaller proportion of income is being spent close to the area in which it is produced and that a larger proportion will be spent in a more distant, more urbanized center.

Although no one wishes to suggest turning the clock back and to deprive the country and its inhabitants of the benefits of economic progress, a realistic appraisal of these obstacles to development is the first step toward designing a development policy for local areas.

LABOR FACTOR APPROACHES

As a general proposition there are two principal routes that can be taken in conducing economic growth. One is an approach facilitating labor factor adjustments including investments in the human agent, and the other pertains to capital investments, per se. Even though it is impossible to separate the two, given their importance in agriculture and elsewhere, it is useful for our analysis to so separate these two economic forces. In general, this discussion will not emphasize the role of land although investments in land will be thought of as being capital investments. If we are willing to accept the existing institutional setup in the United States as given, the pronounced and real disparities in income rewards to the labor factor between farm and rural families and urban families is indicative of a transitional phase toward a long run equilibrium.

Other evidence of this existing disequilibrium is the age distribution found in small communities. The small proportions of population in age categories from about age 18 to age 35 reflect the history of high levels of employment beginning in the early 1940's.

Prior to that time, although there was a net diminution of farm population, even during the late 1930's these diminutions were generally not sufficient to cause disproportionate or imbalanced age distributions for the smaller communities. Impediments in the form of labor force restrictions for persons over 35 and the greater cost of movement on the part of established family members have militated against the outmigration path for many older persons presently in small communities. So that, if we were looking for a long run equilibrium, given current institutional arrangements and seniority and other nonmarket allocation of job opportunities, we could, as a first approximation, hardly expect a long run equilibrium in much less than 25 years, in other words, 1985 or thereabouts. Such an equilibrium would envision the simple effect of the ageing process and the disappearance of persons from the labor force from natural causes.

There is increasing evidence that the urban areas will be increasingly handicapped in the absorption of rural youth as they reach working age. Even with the large reduction in the number of young adults in rural areas, we must still recognize that the fertility ratio in rural areas continues to be higher than that manifested in urban areas. That means that a truly long-run equilibrium would have to take this differential fertility relationship into account.

Considering the high rates of unemployment in urban centers during the past four or five years, particularly among younger workers, the prognosis of the continuing absorption of rural youth as they enter working ages appears to be dimming. Countercyclical policies have not been able to get us very far below a five percent unemployment rate for very long. Moreover the rates of growth have nowhere reached the optimistic levels frequently discussed in the

past. All this amounts to saying that if countercyclical and growth policies continue to function inadequately, another group of rural youth will be isolated in smaller areas away from the full benefits of our national labor market. Furthermore, the long run equilibrium date suggested above will have to be postponed to an even more distant one, perhaps beyond the end of the century.

It is perhaps unfortunate that a number of policies which at least superficially appear to help income and welfare positions of working persons may have unfortunate side affects. Some economists have asserted that the minimum wage law is one. Others have maintained that industry-wide collective bargaining agreements also have unfortunate side effects as they affect the rural and small-town person. Although I will not belabor the analysis of these facts, it seems to me that those persons and groups which may be adversely affected by these policies should look into them more closely. Very little empirical work has been done in this field despite its importance to national and regional economies.

If one adopts the philosophy that these or other institutional arrangements cannot be changed, then one is increasingly forced to move into the arena of capital investment in seeking a solution to the low income problem affecting many local areas. It is in this sense that the investment in the human agent becomes so important for local areas.

It is obvious that the most abundant and valuable resource available to rural and small-town areas is its people. Moreover, it is true that despite all of the strides we as a nation have made in the area of educational and health investment, we still have a long way to go. Unfortunately, it is

the rural areas which are most disadvantaged in providing what might be called "parity investment in the human agent" as compared with urban persons. The statistics pertaining to low levels of educational attainment, low educational quality, and lower indices of health are too well known for us to belabor here. It must, however, strike most observers as somewhat ironic to find that the very areas with the highest rates of natural increase and the highest dependency burden are the very areas in which investments in people are most severely limited. One of the very important effects which local areas must reexamine in developing themselves is this whole process of the investment in the human agent.

Although much can be done and is being done in both these areas on a private basis, it is nonetheless true that the role of public expenditures in the field of health and education is historically very well established. For this reason, equalization formulas for bringing superior educational opportunities to less advanced parts of the state should be examined with favor. Although the basic economic reasoning is the same with respect to national considerations of educational investment, this topic is something so central to political discussion that I shall not attempt to analyze it. However, I should like to point out that without a state equalization system any national equalization could be merely an exercise in words.

It is most important to recognize that the existing policies at the national level in the field of vocational education are being used inadequately by many local communities. I refer particularly to the educational and training opportunities embodied in the Area Redevelopment Act and the Manpower Development and Training Act. These Acts could be improved from

the rural viewpoint by certain amendments and changes to provide a useful means of aiding the investment in rural people. Although it is sometimes claimed that many states cannot utilize these funds freely because of cultural implications, I wish to emphasize that the education and training are provided at the adult level for direct and immediate vocational purposes. It is not directed to children in their formative years, nor for studies in civics or in the humanities.

CAPITAL FACTOR CONSIDERATIONS

Apart from varying capital capacities for investments in the human agent, local communities have a varying capacity for the formation of investment capital. Still further, they vary in their need for other capital. The salient guide with respect to these needs is the existence of profitable investments at the individual firm level.

One of the very important considerations with respect to capital availability in any community is the availability of commercial banking credit. In this regard, local communities are highly disadvantaged. For example, for the 900 United States counties in which there is no population center with more than 2,500 persons, per capita bank deposits amounted to only $731. In the next largest group of counties, those with the largest population center between 2,500 and 9,999 people, the per capita level of bank deposits was $785--seven percent larger, but still small. The still greater availability of bank deposits in metropolitan communities is well known and need not be further explored here. The point to be remembered is that ordinary commercial credit availability is severely limited in communities of small sizes. This credit stringency exists despite the

preferential fractional reserve requirements applicable to country banks. Actually the term country banks may apply to banks in cities of as large as one-half million population under certain circumstances, so that this benefit is not confined to small towns. The low rate of deposits is, in itself, evidence of the insufficiency of this program for smaller communities.

It may be argued that short-term commercial credit is not so meaningful a consideration with respect to many capital-using industries and endeavors as is long-term capital availability. The available data for per capita public debt outstanding on a local basis provides a basis for comparison. Again an important difference will be found--$95 as against $120 per capita. We know, too, that the access of small businesses and enterprises to long term capital markets is quite restricted, so that potential small firms ordinarily attract very little attention from a promoter who operates through metropolitan money markets. This means that the local community which endeavors to attract industry must look to other available sources for its capital.

One such possibility is the use of reinvested earnings in the hands of large multi-plant corporations. It is common knowledge that the locational decisions of many corporations permit location in smaller communities. Even though it is the opinion of a number of economists that many business managers in such companies are often not fully alerted to the possibility of cost reduction which relocation makes possible, one must recall that any relocation decisions require the disinvestment of capital resources in the existing site before movement can, as a practical matter, be considered. Nevertheless, numerous complaints coming from communities in high cost

areas which have lost industry are on record. This indicates that relocation at least in the long run, offers a ray of hope for local communities with lower costs. If the history of the southward movement of the textile industry is a case in point, the long run may indeed be a long one.

Because of the social cost of relocation, it is often considered desirable to attract new rather than relocated plants. The creation of such new plants depends upon various aspects of national economy, for example, the rate of growth of the entire national economy, population relocation, and regional differences in the rates of growth. Other policies, such as commercial policy--the degree to which the United States frees or closes its import gates--tax policy, and the general location and employment policies are all relevant.

An important part of the role of the local community in a situation of either relocation or expansion is to make sure that information regarding cost advantages of its situation are made known to responsible decision-makers.

The local community may not be able to find a multi-plant corporation which is willing to take advantage of a local cost pattern. In such cases some communities have tried to develop organizations which will marshall capital resources for this purpose. This may be done through the organization of a local development commission. Frequently such a commission will erect a plant facility, adapted for a wide range of uses, to be available for a potential entrepreneur.

The entrepreneur who is likely to take advantage of such an opportunity is typically one whose capital is insufficient to make such a capital himself either through reinvested earnings or other capital

accumulation. As a matter of fact, he may well have occupied a loft or other rented facility in a larger community simply because he could not find adequate rental facilities available in smaller communities. This type of "shell building" thus provides a useful means of bringing additional employment opportunities together with a capital contribution in the form of machinery, equipment, and inventory into the local community. It also brings experience with modern production techniques into smaller towns.

Permissive legislation has allowed local communities to utilize their credit capacity to do similar things. In some cases the community's credit capacity can be committed only to the extent of the rentals obtained from their leasing of such structures. In other words, the community's direct taxing power may not be pledged. In addition some communities have made outright gifts of lands, constructed streets and utility connections, forgiven local taxes, and done a number of things to encourage local industrialization. All of these methods appear to me to highlight the very important capital stringency frequently observed in local areas. Many problems confronting local communities derive from imperfections affecting their capital market. Even though some of these attempts to attract further capital may appear to be crude and contrived, they still serve to open opportunities that have hitherto been unexploited.

RELATIVE MERITS OF CAPITAL VERSUS LABOR APPROACHES

Some economists claim that local areas are frequently disadvantaged by certain manifestations of national economic policy--for example, minimum wage legislation and industry-wide collective bargaining. It is quite likely that these policies often adversely affect local areas seeking to develop themselves. However, most observers make a political judgement that the change of these policies is not likely to occur.

On the other hand, there are certain labor policies which would tend to augment the outflow of labor from rural areas, for example, better employment information service and assistance for moving. In this case the policies suggested would serve to accelerate the population loss in the affected areas.

Because of the nature of some of these policies, there has been an emphasis upon policies which make better utilization of existing local capital resources and existing opportunities for the use of public funds. These possibilities, of course, are not independent of labor resource considerations. As a matter of fact a significant proportion of the capital investment problem relates to the investment in the human agent. It is precisely in this area of education and training that the local community can operate effectively. It is, of course, true that an increase in educational budget can also accelerate a population exodus. On the other hand, the upgrading of educational standards, both in general and vocational terms, provides one of the most useful advances for the development of local opportunities. In most rural communities the most abundant and under used resource is the labor resource. Upgrading can help to make a better utilization of labor possible. One of the prime necessities for attracting new industry can be found in the existence of an alert and already trained labor force.

The Federal Government has several very useful programs which can be of help to local communities. These may be listed as follows: The National Vocational Education Acts, the Area Redevelopment Act, and the Manpower Development and Training Act. I will not discuss the details of these programs but I will indicate that they make possible, in order, area vocational schools, 16 week's training in anticipation of the arrival of new industry, and one year's training plus family allowances for low income farm people desiring to upgrade themselves.

It is true, of course, that educational endeavors do not have to wait upon action by the national Government. Here, however, is a ready source of funds and the failure to use these funds on the part of many areas of low income deserves special attention. In large part, perhaps, the small use made of these programs in rural areas may reflect unfamiliarity with the program in small communities and its primary emphasis upon large population centers.

Another possibility for the use of available education funds in local areas is a reorientation of education in the local public schools to give greater emphasis to the kinds of training that will be useful for potential new industries. It is a well known fact nowadays that only a small proportion of the children of farm families can hope to make an adequate living in agriculture. Nonetheless, many communities still emphasize vocational agriculture rather than the kind of training that appears more useful for today's needs. Teachers of vocational agriculture have a real opportunity here to broaden their offerings, and so take an even more important place in their communities.

Although the role of educational investment is extremely important, it is an area of expenditure that requires rather long time for fruition. In this connection we should make a conscious appraisal of local capital sources to do everything possible to provide attractive investment opportunities in the local communities. The low level of commercial bank deposits in smaller communities indicates, in all probability, that there is a constant net outflow of capital funds from these areas. In other words some of the capital formed in a particular area will be used to benefit other communities--many of which are probably less needful.

Some of these flows of capital can no doubt be explained in terms of the unavailability of local investment opportunities and of financial intermediaries. As a consequence much capital is invested in debt instruments and other capital forms which support entities well outside the local area. This adverse capital flow is something that every local community must scrutinize. Probably community lenders in most small communities will be surprised at the extent to which capital flows outward rather than inward. Awareness of this phenomenon can lead to the development of a superior development performance.

In addition to the local sources of capital more attention needs to be given to the process of attracting capital from outside. Although I know that the branch plant effort is extremely popular as a form of this kind of attraction, I would like to emphasize the possibility of new entrepreneurship. Among the possibilities for developing such capital and entrepreneurial assets, local laws for the development of intrastate security promotion may well be examined.

In addition to corporate financing, the financing provided by cooperatives is also welcome. In many ways cooperatives are especially advantageous for the smaller community. They provide a useful means of marshalling local capital and entrepreneurial capacity.

In addition to private sources, the availability of public funds constitutes another and very important source. The Area Redevelopment Act, as is now well known, provides such funds for certain designated areas. Such funds may be used for either public facilities or for the encouragement of private facilities. Still further, the Accelerated Public Works Act of 1962

explicitly provides for public expenditures in designated areas of low income. All in all, the opportunities for uses of capital are not small. It remains for the local community to find time to organize local capital resources and knowledge to its own advantage.

CONCLUSIONS

These comments began with an optimistic note and they end the same way. The old prospector's adage, "Gold is where you find it.", applies to our situation. In the last century the prospecting for gold often brought surprising results. Unlike silver and other metals, the finding of gold did not conform so completely to the geological science of that day. For this reason, gold was discovered in unlikely places.

It is important today for us to be careful in our interpretation of known economic facts. Overall and general tendencies express just that--tendencies, not necessary and sufficient conditions. The necessary and sufficient conditions center on the economics of the individual firm--its ability to cover costs and make a profit. Let nothing in the form of an offhand observation make you forget that. There are thousands of flourishing enterprises in small communities. There are also thousands of foregone opportunities. Gold is there, you may be sure.